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DIRECTORATE OF
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OSD REVIEW COMPLETE

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Arab States: Both Iraq and Syria have publicly attacked the US peace initiative [REDACTED]

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Pronouncements by Syrian officials and the government-controlled press have categorically rejected the US plan, as they have consistently rejected the Security Council resolution on which it is based. Nevertheless, a certain amount of ambiguity has crept into this public position. On 28 July, for example, Syrian leader Atasi met with Nasir's personal representative, who later announced that the meeting was "extremely successful" and that there was "full agreement on all matters discussed."

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The Iraqi rejection of the US move has been uncompromising--presumably a reflection of the fact that Iraq lost no territory in the 1967 war and therefore has nothing to gain in any settlement. Its attitude would be of little importance were it not for the presence of some 20,000 Iraqi troops in Jordan. Recent rhetoric over Baghdad radio has given rise to press reports that Iraq has placed these forces at the disposal of the fedayeen, but the broadcast seems to have been misinterpreted.

Baghdad is no doubt delighted to be able to portray both Husayn and Nasir as traitors to the Arab cause, but it is unlikely to use its troops in Jordan in an actual move against King Husayn.

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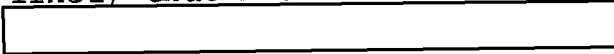
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Palestine Liberation Organization chairman Yasir Arafat is expected to set forth the fedayeen position on the US peace initiative today. A commando spokesman in Amman announced yesterday that the fedayeen leader would also touch upon Egypt's recent decision to cut off guerrilla broadcasts from Cairo. Arafat's stand is likely to be negative on both subjects. Because of President Nasir's great popularity among the Arab masses, however, it is unlikely that Arafat will attack him personally.



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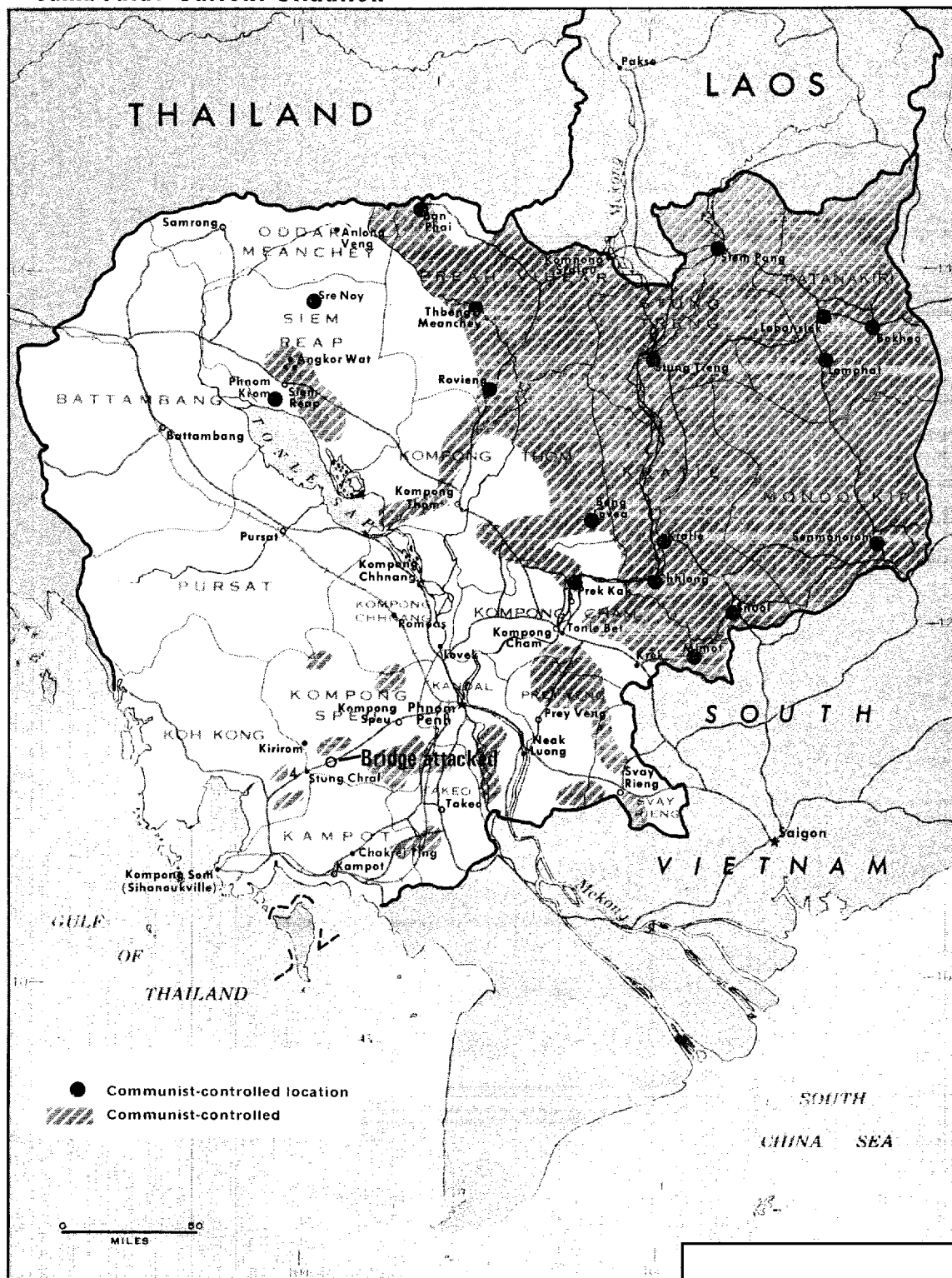
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Cambodia: Current Situation



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Cambodia: The lull in significant military activity continues.

The government counteroffensive to retake Kirirom, spearheaded by five fresh battalions, is moving ahead slowly. Progress was checked yesterday when the Communists blocked the one access road to the town. A small enemy force also attacked a bridge on Route 4, east of Kirirom, on the night of 29-30 July, closing it to heavy traffic.

Most of the troops that retreated from Kirirom on 28 July apparently were in no condition for more combat, and have been withdrawn. The Cambodian commander directing the current operation told journalists that he has asked for US air support because South Vietnamese close air strikes are inaccurate. The continuing poor weather at Kirirom probably will greatly reduce the effectiveness of air support in any event.

The immediate purpose of the Communists' campaign around Kirirom may be more for psychological effect than for significant military advantage. The rugged terrain and the restricted overland access to the town make it an ideal site for prolonged combat, with government troops now forced literally to wage an uphill battle to retake it. The Communists may hope that with a relatively small effort they can demonstrate anew the Cambodian Army's existing tactical shortcomings and at the same time garner more headlines at Phnom Penh's expense.

The continuing presence of a regimental-sized enemy force in the area suggests, however, that the enemy campaign at Kirirom may have some longer range objectives. It may represent, for example, the beginning of an effort to establish a secure rear base of operations in the remote mountainous areas of southwestern Cambodia. Such a base could be used for launching frequent attacks on government positions

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and lines of communication, including Route 4, in the surrounding provinces.

Thai Troop Debate Continues

Foreign Minister Thanat told the press in Bangkok on 30 July that the government would send Thai troops to Cambodia only as "a last resort." He cited the "acrimonious" relations between the Cambodians and South Vietnamese forces operating in Cambodia as an example of the "friction" that can be avoided by keeping Thai troops at home. [REDACTED]

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NATO: The initial stages of the Allied study on defense problems of the 1970s have underlined European opposition to any substantial change in US force levels and in NATO strategy.

The Allies, reacting to a US presentation of the range of possible options regarding US force postures, have strongly favored maintenance of present force deployments. There is general willingness, however, to consider in the Allied defense review how the US could make modest cuts in noncombat areas if some reduction were absolutely necessary. The West Germans, for example, have indicated that they could accept such money-saving steps as a reduction in the NATO stockpiles intended to support a conventional war for 90 days. The Germans also would not be opposed to reductions in the current support system and cutbacks of US troop strength in other European countries.

Strong Allied objections have been raised to any movement away from the current NATO doctrine of flexible response and toward greater reliance on either tactical or strategic nuclear weapons. The Germans have been particularly unequivocal in their opposition to any such change.

The Germans and some other NATO members now believe that in order to retain present US combat force levels, they will have to bear a larger share of the US financial burden. They are examining the possible US force options in this context and will be forwarding additional comments and questions in the course of the upcoming defense review sessions in August.

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Yugoslavia: Joint industrial investments with the West, long sought by the Yugoslavs, are moving ahead.

Daimler-Benz-Mercedes reportedly has agreed to invest \$40 million in a Yugoslav firm for joint production of Mercedes trucks and buses in Belgrade. This agreement is the eighth involving West European automotive assembly operations in Yugoslavia. In addition, a \$10-million joint investment agreement with Renault as well as a large one with Ford are in the offing. Joint investments in other industries have recently been agreed upon with US, Swedish, and Danish firms.

Many of these recent arrangements envisage markets in hard currency areas, so that investors will be able to earn foreign exchange. This probably was a major inducement to Western firms to invest hard currency in joint projects despite other difficulties that have limited foreign investment in Yugoslavia. High taxes and limits on transferability of capital are especially unattractive. Yugoslav businessmen have been pressing the government for several months to liberalize these regulations, and some changes may be made. The requirement for re-investment of some profits in Yugoslavia was recently liberalized.

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Bolivia: President Ovando's latest attempts to placate the left appear to have embroiled him in new difficulties with the military.

The apparently rigged resignation of Information Minister Bailey and Ovando's less than straightforward handling of the student crisis may have created a breach with the military high command that will be extremely difficult to repair. [REDACTED]

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Bailey's resignation last Monday appears to have been a ploy to undercut the military high command by providing a platform for denouncing them as counter-revolutionaries. Similarly, Ovando's rejection of the resignation the following day may have been intended to demonstrate his determination to continue his "revolution," as well as his defiance of military pressure to remove the leftist minister.

Ovando also apparently ignored military desires when he forced through a solution to the growing student problem with an agreement that seems calculated to assure leftists of continued control of the University of San Andres. The agreement, which calls for returning the university to leftist control and then holding student elections, is reportedly viewed as a betrayal by both the conservative students and the military.

A showdown between Ovando and the military now seems inevitable, but it may be delayed by the death of the President's son in a plane crash on 29 July.

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Peru: The long-awaited industrial reform appears to offer scant hope of moderation in President Velasco's "revolution."

The new law was described by Velasco in his independence day speech on 28 July. It is considerably more radical than generally expected. Velasco said that industrial reform would provide for: state control of basic industry; diversion of 25 percent of profits before taxes for distribution to employees and the purchase of company stock for a new workers' organization to be set up; worker participation in management; and a maximum of 33-percent foreign ownership in a company after the original investment is recovered and a "reasonable profit" has been obtained. Foreign ownership apparently could range as high as 49 percent if it were a joint venture with Peruvians.

Optimism among businessmen in Lima had been increasing in recent weeks as it appeared that their representations to the government on the industrial reforms would be reflected in the final law. The promulgation of a law that is even more radical than the original draft, which had already alarmed the business community, however, probably will cause business and investor confidence to sink to a new low.

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Central America - Eastern Europe: Some Central American countries show signs of abandoning their traditionally cool policy toward Eastern Europe.

Central American governments evidently have kept a careful eye on Costa Rican President Figueres' open door policy toward Communist countries. [REDACTED]

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Costa Rica has successfully disposed of some surplus coffee through a commercial agreement with the Soviets, and Figueres has moved the country toward closer relations with other East European nations. Guatemala also is considering establishing commercial relations with the Communist countries to sell coffee and to save money by eliminating middle men.

Most Central Americans remain reluctant to admit Communist personnel for long periods of time. Costa Rica, however, has negotiated to buy on credit Soviet road maintenance equipment that would involve technical instructors, and the bilateral agreement awaiting congressional ratification calls for the exchange of six-man trade missions.

Although Figueres expects quick ratification, his cordiality toward Eastern Europe has been a matter of public controversy at home; much of the public media has been strongly negative. He has nevertheless established diplomatic relations with Romania and Hungary, and is believed to be moving toward exchanges with East Germany, Bulgaria, and the USSR. If the other countries in Central America believe that Costa Rica is able to negotiate favorable deals with Eastern Europe, they are likely to follow suit.

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